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## **FEDERAL MARITIME COMMISSION**

### **46 CFR Parts 501 and 540**

**Docket No. 11 - 16**

**RIN: 3072-AC45**

### **Passenger Vessel Operator Financial Responsibility Requirements for Nonperformance of Transportation**

**AGENCY:** Federal Maritime Commission.

**ACTION:** Final Rule.

**SUMMARY:** The Federal Maritime Commission amends its rules regarding the establishment of passenger vessel financial responsibility for nonperformance of transportation. The amount of coverage required for performance is modified to increase the cap on required performance coverage to \$30 million over a two year period and thereafter adjust the cap every two years using the Consumer Price Index; adjust the amount of coverage required for smaller passenger vessel operators by providing for consideration of alternative forms of protection; remove the application form for issuance of certificates of financial responsibility from the Commission's regulations and make it available at its website; add an expiration date to the Certificate (Performance); and make technical adjustments to the regulations.

**DATES:** The Final Rule is effective: April 2, 2013.

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**SUPPLEMENTARY INFORMATION:**

By Notice of Proposed Rulemaking (NPRM) published on September 20, 2011, 76 FR 58227, the Federal Maritime Commission (Commission or FMC) proposed to amend its rules regarding the establishment of passenger vessel financial responsibility under 46 U.S.C. 44102 (formerly contained in section 3(a) of Public Law 89-777).<sup>1</sup> After

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<sup>1</sup> See 46 U.S.C. 44102 (a) through (c).

receipt of public comments responding to the NPRM, the Commission issued a Request for Additional Comments and Information (RFI) relevant to the Commission's analysis whether revision of the Commission's regulations governing passenger vessel operators could have a significant economic impact on a substantial number of small entities.<sup>2</sup>

The Commission adopts the Final Rule as set forth below. Also the Chairman of the Commission certifies below pursuant to section 5 U.S.C. 605(b) of the Regulatory Flexibility Act, 5 U.S.C. 601 *et seq.*, that the Final Rule will not have a significant economic impact on a substantial number of small entities as none of the nine small PVOs that are subject to the Commission's Part 540 regulations are found to be significantly impacted by the changes adopted.

#### Current and Final Rules

The Commission's current rules provide that "[n]o person in the United States may arrange, offer, advertise or provide passage on a vessel unless a Certificate (Performance) has been issued to or covers such person," 46 CFR 540.3. Such persons must apply for a Certificate (Performance), 46 CFR 540.4, and provide financial responsibility "in an amount determined by the Commission to be no less than 110 percent of the unearned passenger revenue of the [PVO] applicant" for the two immediately preceding years, "reflect[ing] the greatest amount of unearned passenger revenue," 46 CFR 540.5.<sup>3</sup> The amount of required financial responsibility, however, is capped at \$15 million. 46 CFR 540.9(j).

Substantive Revisions. The final rule increases the cap on financial responsibility

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<sup>2</sup> Docket No. 11-16, Request for Additional Comments and Information, 77 FR 11995 (February 28, 2012).

<sup>3</sup> "Unearned passenger revenue" is defined as "passenger revenue received for water transportation and all other accommodations, services, and facilities relating thereto not yet performed." 46 CFR 540.2(i).

required of PVOs from \$15 million to \$30 million. The rule includes a phase-in period of two years in order to allow the industry time to adjust. One year after the rule becomes effective the cap increases to \$22 million. The second year after the rule goes into effect the cap increases to \$30 million. Biennially, thereafter, the limit will be adjusted to the nearest \$1 million using the Consumer Price Index for all Urban Consumers (CPI).<sup>4</sup>

Whereas the Supplementary Information of the NPRM provided for notice to be given of any increase in the cap, the proposed rule omitted the notice requirement. The attached final rule includes a formal notice, requiring the Bureau of Certification and Licensing (BCL) to calculate the adjusted cap amount and transmit that information to the Commission's Office of the Secretary (Secretary). The Secretary will then publish the notice of the new amount and the date on which it is to become effective on the Commission's website ([www.fmc.gov](http://www.fmc.gov)) and in the *Federal Register*. The Secretary will establish an effective date that is no less than sixty (60) days after *Federal Register* publication.

The final rule also provides that PVOs with unearned passenger revenue (UPR) that is no more than 150% of the cap (i.e., UPR of \$45,000,000 or less) may request relief from coverage requirements by means of substituting alternative forms of protection. The Final Rule requires that requests be submitted to the Bureau of Certification and Licensing and authorizes the Director of BCL to grant requests based upon the already existing protections applicable to credit card receipts for PVOs whose payment policies provide for final payment by passengers to be made within 60 days of

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<sup>4</sup> The Bureau of Labor Statistics' Consumer Price Index for all Urban Consumers is the most widely used measure to track changes in prices by federal agencies and financial institutions.

the vessel sailing.<sup>5</sup> If such a request is granted, the PVO would meet its coverage requirements by a combination of the substituted financial responsibility alternative and financial responsibility covered by any insurance, guaranty, bond or escrow agreement.

Other Revisions. A number of other revisions are included that refine the rules to address issues and make corrections based upon the staff's experience. For example, the definition of "Unearned passenger revenue" in section 540.2(i) is revised to clarify that UPR "includes port fees and taxes paid" by passengers but excludes "such items as airfare, hotel accommodations, and tour excursions" that passengers also pay for but are not part of the passenger vessel transportation element of the cruise. The matter of whether port fees and taxes must be reimbursed has arisen repeatedly over the years. The staff has consistently advised that such costs are included in the water transportation related costs that are covered within the ambit of the statute and the Commission's regulations. This change will help PVOs and the public to quickly ascertain from the Commission's regulations that these amounts are reimbursable from the financial responsibility established by PVOs.

Sections 540.4(b) and 540.23(a) have been modified to direct applicants to file application form FMC-131 directly with the Bureau of Certification and Licensing, rather than the Office of the Secretary, reflecting actual practice over many years. The Final Rule removes form FMC-131 from the Commission's regulations, instead it will be made available on the Commission's web site ([www.fmc.gov](http://www.fmc.gov)) or from the Bureau of Certification and Licensing.

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<sup>5</sup> Corresponding revisions to sections 501.5(g)(2) and 501.26(d) are made to provide the necessary delegation of authority to BCL to review and grant requests for substituting alternative financial responsibility.

The sample surety bond, guaranty, and escrow agreements that are set forth in the Commission's regulations are also amended and were included in the NPRM for public comment.<sup>6</sup>

Section 540.7 is revised to require that each Certificate (Performance) expires 5 years from the date of issuance. This varies from the current rule that provides that the certificate continues in effect for an indeterminate time. The Final Rule also provides that, for good cause shown, the Commission may issue a certificate with an expiration date less than 5 years.

### Public Comments

#### 1. Comments on the Current and New Caps.

Cruise Lines International Association, Inc. (CLIA) submitted comments on behalf of its members, sixteen of which are PVOs currently in the Commission's program. All sixteen have UPR exceeding the current \$15 million cap. CLIA opined that the current cap of \$15 million was adequate, but did not oppose increasing the cap to \$30 million. CLIA indicated that a \$30 million cap would more than adequately cover the risks of nonperformance. CLIA also does not oppose the use of the CPI to adjust the \$30 million cap every two years.

Lindblad Expeditions, Inc., an operator of U.S. flag passenger vessels under the program, supports increasing the cap "commensurate with the UPR exposure of all PVOs" but indicates that such exposure "would best be accomplished by eliminating the cap altogether." Lindblad supported the adjustment of Part 540 financial responsibility coverage to take into consideration overlapping financial protection provided by credit

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<sup>6</sup> These forms were submitted to the Office of Management and Budget for its review at the time of the NPRM was issued.

card issuers. Specifically, Lindblad recommended the Commission take into account PVO bonds with the U.S. Tour Operator Association and private trip insurance.

American Cruise Lines, Inc. (ACL) (an operator of U.S. flag vessels), InnerSea Discoveries, LLC (InnerSea) (an operator of U.S. flag vessels), Congressman Andy Harris, M.D., the Passenger Vessel Association (PVA) (the national trade association representing owners and operators of U.S. flagged passenger vessels), the National Association of Surety Bond Producers (NASBP) oppose increasing the cap to \$30 million. The Surety & Fidelity Association of America (SFAA) neither supports nor opposes the increase.

ACL, Lindblad, InnerSea, PVA, and Congressman Harris assert that the current cap and increased cap unfairly discriminate against smaller U.S. flagged PVOs as they must devote a large portion of their capital to comply with the financial responsibility requirement of 110% UPR. In contrast, the larger, foreign-flagged PVOs have to cover a much smaller percentage of their UPR. ACL and InnerSea consider their financial responsibility burden to be disproportionate to their risk of non-performance.

NASBP and SFAA advise that, because sureties demand reimbursement for losses, sureties conduct a thorough financial assessment of each PVO in order to assure the PVO has sufficient financial strength for the bond amount sought. NASBP and SFAA expressed concern that a PVO faced with a higher bond amount due to an increase in the cap may not be able to demonstrate financial strength necessary to obtain a bond. NASBP recommends that the Commission eliminate any cap and that a flat 15 percent of UPR be set as the financial responsibility level for all PVOs,

regardless of size. NASBP calculates that the flat rate would produce \$555 million in financial responsibility industry-wide (in comparison to the amount indicated in the Commission's NPRM).

InnerSea proposes that regulations be adopted that concentrate on a PVO's financial stability, regardless of size. InnerSea recommends that financial responsibility be tied to familiar financial ratios, such as debt to equity ratios, when setting coverage levels.

PVA suggests that a two-tier cap be implemented; one that applies a \$15 million cap to PVOs with UPR between \$15 million and \$30 million and a \$30 million cap for those PVOs with UPR of greater than \$30 million. PVA indicates that such a two-tier cap approach would protect small U.S. flagged operators from the adverse impact of the cap increase.

## 2. Comments on Alternative Forms of Financial Responsibility.

ACL, Lindblad, PVA, Royal Caribbean and CLIA all support the concept of alternative protection in order to take into consideration duplicative coverage derived from sources other than the Part 540 financial responsibility. ACL and CLIA assert that such alternative protection should include consideration of credit card sales, given that additional financial protections exist for credit card purchasers under the Fair Credit Billing Act (FCBA), 15 U.S.C 1666(a). CLIA also suggests, in its response to the NPRM, that the U.S. Bankruptcy Code protects passengers. CLIA points to protections provided to unsecured creditors under the Bankruptcy Code priority set out in section 503(a)(7), 11 U.S.C. 503(a)(7), which covers money paid for services that are not



delivered. ACL and Lindblad suggest that the Commission needs to consider factors other than credit cards with respect to alternative forms of protection. Lindblad suggests that travel insurance be considered as alternative protection.

ACL supports reliance upon credit card refunds but cautions that credit card issuers may require increased collateral as further protection. ACL cites an American Express letter dated May 29, 2003 indicating that if the Commission offset bond amounts based upon refunds from credit card sales, then card issuers would “require PVOs to post collateral that covers all UPR charges [made] with the company's credit cards.” PVA expressed a similar concern that if credit card companies perceive increased risk they would alter the terms of their agreements with PVOs. Lindblad indicates that PVOs are required to pay fees and establish cash reserves with a third party which exceeds 10 percent of high UPR.

With respect to the requirement establishing the limitation for making a request at 150 percent of the highest UPR, ACL asserts that such a limit would create a disincentive to growth as smaller PVOs will attempt to assure that their UPR not reach \$45 million in order to continue qualifying for alternative protection consideration. CLIA likewise suggests that the 150 percent limitation is too low and will provide a disincentive for small cruise lines to embark passengers at U.S. ports as their UPR approaches the 150 percent mark.

Congressman Harris and InnerSea oppose reliance upon credit card refunds or travel insurance as sources for alternative financial protection. Echoing other PVOs, cited *supra*, Innersea states that greater industry reliance on credit cards and travel

insurance will result in increased usage costs for these services to offset the increased risk to the credit card and travel insurance providers. InnerSea thus opposes this alternative as detrimental for the cruise industry as a whole.

Congressman Harris asserts that offsetting travel insurance and credit card payments would not eliminate the discriminatory effect against smaller, U.S. flag PVOs. Instead, the likely effect of recognizing such alternative methods is to substitute credit card issuers in place of the Commission as the party demanding increased financial security.

As indicated above, SFAA asserts that because sureties demand reimbursement for losses they conduct a thorough financial assessment of each PVO in order to assure it has sufficient financial strength to reimburse the surety. SFAA suggests that, in analyzing any alternative financial security, the Commission should consider whether the alternative security includes a process that performs a similar prequalification function (as that provided by sureties) as well as providing sufficient financial protection in the event the PVO defaults.

### 3. Other Comments.

ACL and CLIA both recommend eliminating the 10 percent “administrative fee” for PVOs below the \$30 million cap. ACL asserts that it should be eliminated as it “is intended to cover the cost of administration” of the Commission’s “nonperformance financial security program” and that there is no sound basis for it being imposed on smaller U.S. flag coastwise trade PVOs and not on the larger PVOs that meet the cap. Similarly, CLIA suggests the “administrative fee” be eliminated as requiring 100 percent

of UPR is burdensome enough without the added 10 percent.

The NPRM also requested comment as to whether a model similar to PVO casualty requirements employing the number of berths on a PVO's largest vessel might be appropriate for the nonperformance program. ACL supports the idea from the standpoint that it would appear to eliminate the cap but is concerned whether it would foster growth in the industry. CLIA opposes a casualty model, asserting that Congress specifically created a model of financial security for death or injury and created a very different model for nonperformance. CLIA points out that Congress created the casualty provisions at the same time it created the nonperformance requirements of Public Law 89-777 and, in doing so, manifested a clear intention that the claims be treated differently.

Carnival suggests that financially sound PVOs that have a number of cruise brands be treated as a single applicant for purposes of the financial responsibility requirements. Carnival recommends that such applicants be covered by a single \$50 million bond backed by the parent company's guaranty. Carnival explains that such a bond and parental guaranty would provide greater security by assuring that the parent stands behind its group of companies.

### Discussion

#### The \$30 Million Cap.

Those opposing the increase in the cap are ACL and the PVA, which represents U.S. flag passenger vessel operators, including ACL, InnerSea and Lindblad. Their comments focus on the disparity between the 110 percent of UPR that they must secure

versus the large PVOs, with UPR exceeding the current and increased cap limitations. Commission-mandated coverage for large PVOs has been capped for 20 years at \$15 million and, under the final rule, will rise to \$30 million. The comments underscore that small U.S. flag PVOs are particularly disadvantaged because they must operate vessels meeting U.S. build limitations and must hire U.S. crews, neither of which burden the large foreign flag PVOs. Congressman Harris shares this concern.

These comments accurately reflect that the large PVOs that qualify for the current cap have enjoyed unchanging financial responsibility burdens for all of their UPR above \$15 million for 20 years. In contrast, smaller PVOs' financial responsibility requirements have been subject to increases during those 20 years, as their high two-year reported UPR increased. Those opposing the new cap do not see the increase as a change that meaningfully narrows the gap between the 110% financial responsibility requirements applicable to small PVOs vis-a-vis the small fraction of financial responsibility required of much larger PVOs.

It is clear that the larger PVOs with UPR exceeding the current cap have had the benefit of an unchanging burden of financial responsibility for the past twenty years; during this same period the PVO industry's highest UPR quadrupled from \$1 billion to approximately \$4 billion. In effect, the overall financial burdens of the Commission's requirements have diminished over time as the percentage of the UPR covered by financial responsibility dropped from 25% to 7.9% of UPR.<sup>7</sup>

The \$30 million cap will result in a significant increase in the UPR covered by

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<sup>7</sup> In 1990, the total financial coverage provided was nearly 25% of outstanding UPR, amounting to slightly more than \$250 million. With the total two-year high UPR for all PVOs in the Commission's program now at approximately \$4 billion, only 8% of UPR (\$323 million) is covered by financial responsibility.

PVOs' financial responsibility, with the preponderance of the increase falling on large PVOs. Based upon the recent reported UPR of PVOs providing nonperformance coverage, it appears that coverage requirements for fifteen of the large PVOs would increase to \$30 million, increasing total coverage for the industry by \$225 million. This would increase industry-wide coverage requirements to approximately 13.5 percent of outstanding UPR.

Without recognition of alternative forms of coverage, three of the commenting PVOs that benefit from the current cap would be immediately impacted by adoption of the rule, as they would be subject to increasing their financial responsibility. However, alternative forms of coverage, discussed below, would potentially reduce their coverage requirements below the \$15 million currently maintained by these PVOs.

Adoption of the \$30 million cap on the basis of the quadrupling of UPR for the largest PVOs over the past 20 years is sufficient reason for increasing the cap. However, the Commission has, in the past, found the effects of inflation are relevant to increasing the cap.<sup>8</sup> In Docket No. 90-01, the Commission stated that the increase was "predicated, for the most part, upon the increase in the consumer price index."<sup>9</sup> Since 1967, when the cap was set at \$5 million, the Consumer Price Index has increased more than five-fold. Use of the CPI, adjusted from the last increase in 1990, would equate to a cap of over \$25 million. Yet, as described, the amount of UPR that is outstanding, and thus passenger monies at risk, has increased much more than general inflation based upon the CPI.

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<sup>8</sup> Docket No. 79-93, Final Rule, 45 FR 23428 (April 7, 1980) and Docket No. 90-01, Final Rule, 55 FR 34564 (August 23, 1990).

<sup>9</sup> Docket No. 90-01, Final Rule, 55 FR 34564, 34566 (August 23, 1990).

The Commission adopts the increased cap based upon the large increase of UPR of large PVOs over the last twenty years with no increase in the cap. The Commission also adopts the requirement that the \$30 million cap will be adjusted every two years based upon the CPI-U. Based on past history, the use of the CPI-U would not account for all of the increase in UPR of the largest PVOs, but will serve to capture some of the increases in large PVOs' UPR.

As described above, the final rule is amended to provide notice of each biennial cap adjustment. The final rule provides that: (1) the Bureau of Certification and Licensing will calculate the adjusted cap amount and transmit that information to the Secretary; and (2) the Secretary will then publish in the *Federal Register* and the Commission's website notice of the new amount and its effective date. The Secretary will establish an effective date for the new cap that is no less than sixty (60) days after *Federal Register* publication.

The suggestions by NASBP (that a flat 15% of UPR financial responsibility requirement be set for all PVOs), by InnerSea (that all PVOs' financial responsibility be established using familiar financial ratios such as debt/equity), and by PVA (that a two-tier cap system be put in place) create concerns and uncertainty that the final rule avoids. Application of the NASBP's flat 15% would apply a low and potentially inadequate percentage to all PVOs that do not meet the current \$15 million cap. Inasmuch as 12 of the 15 PVOs that have ceased operations since September 2000 were PVOs whose UPR was below that threshold, the Commission's experience is that smaller PVOs have greater risks that performance coverage will be required to

reimburse passengers for losses. Without current coverage requirements, many passengers would have suffered significant losses.

InnerSea's suggestion that regulations should concentrate on a PVO's financial stability, regardless of size, would seem similarly problematic. The Commission would need to define what sound financial health means and then conduct thorough and intrusive financial reviews to determine "financial health." Experience has shown that financial reports significantly lag actual events. Under InnerSea's suggestion, upon discovering a PVO no longer was of sound financial health, the Commission would likely be faced with the quandary of increasing coverage requirements at a time that would potentially expedite the PVO's financial failure, or risk standing by while the PVO fails and leaves customers financially imperiled.

Those suggestions would require the Commission to continuously monitor the financial health of every PVO. Financial reports not required to be filed currently would of necessity be mandated. The Commission's previous experience with American Classic Voyages Company (American Classic), when it ceased operating, demonstrated the short comings of reporting requirements as well as the inadequacy of self-insurance as a means for PVOs to meet their financial responsibility requirements. See Financial Responsibility Requirements for Nonperformance of Transportation – Discontinuance of Self-Insurance and the Sliding Scale, and Guarantor Limitations, 29 SRR 685 (June 26, 2002). The Commission noted that "experience demonstrates that the lag time in receiving financial data may prevent the Commission from knowing about a PVO's financial deterioration until well after it is too late to remedy the lack of coverage." *Id.* at

688.

PVA's suggestion of a two-tier cap system would leave the \$15 million cap in place for those PVOs with up to \$30 million in UPR. While this would provide greater certainty, it would also necessitate a significant increase in requirements at the point \$30 million UPR is reached. A PVO would move immediately from a \$15 million cap to a \$30 million cap. The Commission's final rule allows for alternative forms of coverage for those whose UPR is less than \$45 million and provides greater relief to smaller operators, such as those represented by PVA.

The Commission's experience with respect to PVOs that have ceased operation is relevant to consideration of the \$30 million cap and to consideration of individual proposals for alternative financial protection, provided the PVO's UPR is less than 150% of the cap. For example, American Classic had UPR of \$51 million.<sup>10</sup> Approximately 60% of American Classic's passengers were reimbursed through credit card issuers and travel insurance. Only after ten years of bankruptcy proceedings did the remaining 40% of the American Classic passengers, specifically, those who had paid by cash or check, finally receive reimbursement of up to \$2,100 each. The \$2,100 reimbursement was the maximum amount provided for under the Bankruptcy Code priority applicable at the time.

CLIA indicated, in its response to the NOI, that it understood most of American Classic's passengers received full "Fair Credit Billing Act . . . refunds" and refunds via

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<sup>10</sup> Fifteen PVOs covered by the Commission's regulations have ceased operations since 2000. They were: Premier Cruise Operations Ltd. (Premier), New Commodore Cruise Lines Limited (New Commodore), Cape Canaveral Cruise Lines, Inc., MP FerryMar, Inc., American Classic, Royal Olympic, Regal Cruises, Ocean Club Cruise Line, Society Expeditions, Scotia Prince, Glacier Bay, Great American Rivers, RiverBarge Excursion Lines, Inc., Majestic America Line and West Travel, Inc. d/b/a Cruise West.



the bankruptcy process. CLIA stated that the passengers of one American Classic vessel received “100 percent of their fare payments through the bankruptcy process within 17-18 months after the [American Classic] bankruptcy filing.” However, according to the bankruptcy plan administrator’s office, the 40% of passengers who paid by cash or check were classified as priority claimants in the bankruptcy proceeding and received only the maximum amount available under the bankruptcy code for that category of customer deposits, which was \$2100 per person at that time. If any individual passengers’ deposit equaled more than \$2100 per person, they would not have been fully reimbursed via the American Classic bankruptcy proceeding. With respect to passengers of the American Classic vessel M.S. PATRIOT, a compromise was structured after extensive negotiations whereby the passengers received reimbursements of 26% of their initial deposits.

#### Requests for Substitution of Alternative Forms of Financial Protection.

The final rule provides a process by which a PVO whose UPR is less than 150% of the \$30 million cap (i.e., \$45 million) may request relief from the Commission by seeking recognition of additional financial protection(s) in substitution for coverage otherwise required by the Commission’s regulations. This case-by-case process is supported broadly by the vessel interests that submitted comments. Alternative sources suggested include recognition of existing credit card refund requirements (whether under the Fair Credit Billing Act or not), Bankruptcy Code priorities that allow recovery of consumer deposits made for services rendered but not performed, private travel

insurance, and U.S. Tour Operator Association (USTOA) performance bonds that are purchased by some PVOs.

Several commenters indicate, however, that reliance on credit card refunds can be problematic in that, if the Commission grants a request, the credit card companies could increase security to cover some or all of the UPR relief granted. This could include hold-backs or letters of credit to protect the credit card company in the event of nonperformance. One commenter, InnerSea, indicates this outcome is a near-certainty.

The Commission has rarely recognized alternative forms of financial responsibility. The Commission decided to grant a request by a PVO for relief from the otherwise applicable financial responsibility requirements pursuant to 46 CFR 540.5. The Commission accepted credit card receipts and the PVO's USTOA performance bond in recognition of the increased collateralization by its credit card company requiring funds to be held back to cover nonperformance. Since credit card issuers had set up a separate escrow type fund to protect its cardholders, it was deemed unnecessary to mandate a duplicate escrow set up under Commission regulations. A concern with the relief given to the PVO, however, was that the "hold-back" funds also would be available to be used to reimburse the passenger for services unrelated to the ocean transportation, including air fare, shore excursions, port transfer and baggage charges.

Comments responding to the NOI, NPRM and RFI indicate that PVO credit card receipts account for 50 percent to 94 percent of passenger fares. The concern was expressed that credit card sales in effect result in double coverage because some are

required by the card companies to provide collateral and pay extra fees in addition to the costs associated with obtaining financial responsibility to comply with the Commission's regulations in Part 540. Though the extra collateral and fees may be used to refund unearned revenues that fall under the Commission's regulations, credit card refunds are not limited to payment of the unearned revenues covered by Part 540.

With respect to the consumer protections under the Fair Credit Billing Act, the cardholder must give written notice of non-performance to the card issuer within sixty days after the credit card issuer mailed the statement containing the charges. See Federal Trade Commission Letter, addressed to the Commission's General Counsel dated November 16, 2010. Though credit card issuers must give such refunds for billing error claims received within that 60-day window, they do not appear to be legally required to make refunds for written claims notified after 60 days of transmittal of billing statements.

As indicated in comments, common PVO industry practice requires full payment of cruise fares from 60 to 90 days prior to sailing, though booking usually occurs months before the sailing date. Passengers may be required to make substantial initial deposits at the time of booking. Such booking deposits may account for up to 30 percent of the total fare. Hence, booking deposits made by credit cards normally do not fall within the 60 day window of the FCBA. CLIA indicates in its response to the NOI, however, that approximately 50 percent of cruise fares are paid within the 60-day FCBA window.

Notwithstanding that credit card companies have consistently reimbursed cardholders, even where nonperformance occurred beyond the 60-day window, the

increased reliance on credit card refunds as an alternative form of protection can present other concerns. For example, credit cardholder contracts vary by card issuer and cardholder, and are subject to unilateral changes by the card issuer; the Commission has no authority to assure that credit card issuers will make Part 540 refunds in preference to other non-statutory claims associated with passengers' broader travel plans (e.g., hotels, airfare, land-side excursions, etc.). There is no assurance that the card issuer will make such reimbursements in certain circumstances or, as a general matter, continue to make such refunds. Nonetheless, recognition of credit card protection may serve, on a case-by-case basis, as the primary source of alternative financial responsibility.

Credit card reimbursement requirements and policies exist regardless of Commission requirements. Such requirements may be imposed by statute, regulation or policies of credit card issuers. Consideration of credit card protections by the Commission does not change those requirements. However, it is true that credit card issuers may require collateral based upon a risk assessment of a PVO or other company. Nonetheless, imposition of such a requirement presumably is based on the perceived risk of failure of the enterprise. That risk would exist whether or not the Commission required additional coverage.<sup>11</sup> Accordingly, requests to provide alternative financial responsibility based upon credit card reimbursements may be granted but the amount of such protection to be recognized will be determined on a case-by-case basis.

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<sup>11</sup> Of note, Commission filed bonds and guaranties historically have paid reimbursements only after existing protections have been exhausted. As credit card issuers have been found not to have subrogation rights to such instruments, they are responsible irrespective of Commission requirements.

Private travel insurance policies differ widely. For example, some policies only reimburse passengers in the event the PVO formally declares bankruptcy. Others will reimburse passengers only after the PVO officially announces that it has suspended operations due to insolvency or bankruptcy. Still others may not cover nonperformance by the PVO, but only the inability of the passenger to travel as scheduled. Some PVOs offer travel insurance that have portions of coverage which are not in fact underwritten by insurance providers, with the passenger protected only to the extent of the PVO's ability to reimburse.<sup>12</sup>

The wide variability of travel insurance policies makes it difficult for the Commission to assure that the proceeds are adequately and reliably targeted to reimburse passengers for their unperformed water transportation. Therefore, it appears to the Commission that private travel insurance as a form of alternative financial responsibility is not sufficiently reliable at this time to support a request to provide substitute financial responsibility.

The performance bonds that PVOs purchase from the U.S. Tour Operators Association are also suggested as a source of substitute financial responsibility. The Commission has had some experience with respect to the USTOA bond performance. Unlike private travel insurance, the USTOA bond is an agreement between the PVO and the association, not the individual passenger. Also, the USTOA bond varies less from bond to bond and appears to have been administered with consistent results. The

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<sup>12</sup> In addition to the Commission's concerns with one PVO over the use of hold back funds, the Commission learned that private travel insurance offered by the PVO proved illusory. When PVO failed to perform, the passengers were not reimbursed from the "insurance." The premiums paid by passengers to the PVO were gone; as the PVO had used the money for other purposes.

USTOA bond may merit consideration with respect to a request for relief, provided the bond text were amended to provide specifically for coverage of Part 540 unearned revenues; or if amended to provide a mechanism whereby passengers are paid directly, not via the insolvent PVO.

As indicated by passenger experience with respect to the American Classic bankruptcy, it would appear that the Bankruptcy Code priority for services not performed is a source of last resort for refund of unearned passenger revenues. Not only did some American Classic passengers have to wait almost ten years for refunds, some received refunds of only 26 percent. Bankruptcy would, therefore, be an unreliable source of passenger protection. Bankruptcy likely would not be anticipated and, even if a bankruptcy were to occur, there would be no assurance of sufficient assets to reimburse any passenger, much less fully reimburse all of them.

The process provided in the final rule enables the Commission, on a case-by-case basis, to consider additional protections submitted by an applicant. The rule provides that PVOs with UPR not exceeding 150% of the cap may submit requests for relief from coverage requirements by substituting alternative forms of protection. ACL and CLIA both suggest that the 150% level is too low, and that more small PVOs would be able to take advantage of the process if the level were higher. The most significant effect of increasing the percentage would be to lessen the amount of UPR that is covered by established financial instruments under the Commission's nonperformance program in substitution for security that is not as certain, such as credit card refunds.

Currently, 28 of the 40 PVOs in the Commission's program have UPR below

\$45,000,000 and each therefore may qualify for lowering their current coverage requirements. However, raising it to 200% would allow consideration of only one additional PVO. Accordingly, the Commission adopts the 150% threshold for submission of requests for relief.

ACL commented that the Commission did not indicate what criteria governed the process. This point is well taken. Accordingly, the final rule has been amended to set out criteria the Commission will use in considering such requests.

The final rule requires that requests be submitted to the Bureau of Certification and Licensing. PVOs must include their most recently available annual and quarterly reports, irrespective of the alternative financial responsibility upon which a request may be based.

For requests based upon the already existing protections applicable to credit card receipts, the PVO must, for voyages occurring during the most recent twelve months, include: the total deposits and payments received for passenger vessel transportation (whether by cash, checks or credit cards), the total credit card receipts; and a copy of the PVO's policy(ies) governing payments by passengers (i.e., deposits and the number of days prior to sailing the passenger must make final payment).

The final rule provides that the Commission may permit a reduction in financial responsibility to be based upon credit card receipts. The amount of such a reduction is determined by halving the proportion of credit card receipts to the PVO's total receipts, and applying the resulting percentage to the PVO's highest two-year UPR. For example, where the total credit card receipts for the twelve-month period equals 30

percent of the total receipts for the period, the PVO would receive a 15 percent reduction off of its highest UPR. Such requests ordinarily will be granted for PVOs whose payment policies provide for payment within 60 days of the vessel's sailing date and financial condition appears to be sound. Requests based upon payment policies that require final payment more than 60 days from the date of sailing may be granted for a lower percentage reduction. The Director of BCL, may, however, refer such requests to the Commission for decision.

The final rule also provides that the alternative financial responsibility granted will remain in effect until its Certificate (Performance) expires pursuant to 540.7(b) unless the Commission determines otherwise based upon paragraph 5 of this section.

Additionally, BCL may request additional information, at the time of the initial request, from the PVO. Such requests are made now by BCL when, for example, it receives information that may bear on a PVO's ability to perform. Similarly, the final rule adds a provision enabling the BCL to request such information from PVOs after their requests are granted. Of course, the PVO may provide any other information related to the alternative financial responsibility or its financial condition that it considers relevant to its request.

#### Other Matters Raised

ACL and CLIA each suggest elimination of the 10% "administrative fee." They refer to the last ten percent in the 110% of UPR required of PVOs that do not qualify for the cap. ACL asserts that the 10% is used to administer the Commission's nonperformance program. To clarify, the 10% is not an "administrative fee" in any



sense and the Commission does not receive any of the 10%. All 110 percent of a PVO's financial responsibility is devoted to refunds in the event of nonperformance and, in some instances, to cover costs associated with payment of reimbursements, such as standard check processing fees by banks.

Further, in promulgating the original regulations implementing section 3 of Public Law 89-777 in 1967, the Commission established the requirement that PVOs provide financial responsibility equal to 110% of UPR. The Commission stated that the rule is designed to recover 100% of unearned revenue based on two years' performance "to give an indication of the general operating condition of the applicant, plus a safety factor of 10 percent." 32 FR 3986 (March 11, 1967). In short, this 10 percent "safety factor" assures reimbursement where the actual amount of UPR at the time a PVO fails to perform is greater than the amount last reported.

For example, as reflected in the Regulatory Flexibility Act Threshold Analysis described below, escrow agreements are obtained more often by smaller PVOs. Such PVOs may have difficulty obtaining a bond or guaranty or have seasonal services or operations that otherwise experience drastic change in the amount of UPR through the year. Escrow agreements require a fixed 10% to be kept in escrow during the slow season and require that funds received from voyage deposits and final fare payments be deposited on a timely basis into the escrow account. Among other requirements, escrow PVOs are required to submit reports of monies received and deposited on a weekly and monthly basis so that the Commission can confirm that the rapidly accumulating funds have, in fact, been deposited. Most escrow agreements provide

that “the Customer may, at any time, deposit additional funds consisting exclusively of UPR and the Fixed Amount into the Escrow Account.” Hence, the 10 percent safety factor helps bridge gaps between the most recent report of weekly deposits and amounts received but not yet deposited.

As described by ACL and CLIA, their suggestion would result in an “across the board” cut for all PVOs that do not qualify for the cap. The recognition of alternative coverage to reduce current coverage requirements, however, negates the need to consider eliminating the 10% safety factor, as fewer small PVOs may be submitting coverage of 110% of UPR. Therefore in light of the Commission’s experience that significant shortfalls in UPR (deposited and revenue received but not yet deposited) frequently occur with respect to escrow agreements, the 110% coverage requirement remains unchanged for all PVOs, except those that qualify for the \$30 million cap or who receive relief under the new rule providing for substitution of alternative financial responsibility. In any event, escrow agreements will continue to require a minimum of 10 percent to be held in escrow at all times; even where an escrow PVO obtains relief to provide alternative financial responsibility for the remaining 90% of its UPR.

The Commission also requested comment as to whether nonperformance financial responsibility levels might be established using a methodology similar to that for the casualty program for PVO financial responsibility. CLIA commented in response to this suggestion and strongly opposes it, asserting that the casualty methodology was established by statute at the same time, and in the same statute, as the nonperformance provisions, which CLIA asserts indicates that Congress intended

separate and distinct systems for casualty and performance coverage. CLIA's comments imply that new statutory authority would be needed to make such a change. ACL indicated that the idea had some merit but that they would need more information on such a proposal. As the Commission adopts the rule as proposed, there is no need to consider the use of a methodology similar to that for establishing financial responsibility under the Commission's casualty program.

As described above, Carnival suggests that financially sound PVOs that have a number of cruise brands be treated as a single applicant for purposes of the financial responsibility requirements. Carnival recommends that such applicants be covered by a single \$50 million bond backed by the parent company's guaranty. Carnival explains that such a bond and parental guaranty would provide greater security by assuring that the parent stands behind its group of companies. The adoption of the final rule also obviates the need to consider a financial responsibility methodology that would potentially reduce the financial responsibility requirements of larger PVOs.

#### Technical Changes.

The Commission also adopts certain technical changes to its passenger vessel financial responsibility regulations in Part 540. Those changes include the revision of the definition of "unearned passenger revenue" in section 540.2 (i) to clarify that UPR "includes port fees and taxes paid" by passengers but excludes "items as airfare, hotel accommodations, and tour excursions." The wording adopted varies from that contained in the NPRM but reflects the Commission intention to clarify the coverage of the term.

The changes to section 540.4(b) and section 540.23(a) are also adopted. Applicants will file their applications directly with the Bureau of Certification and Licensing instead of with the Office of the Secretary. Form FMC-131 will be deleted from the Code of Federal Regulations and instead made available on the Commission's web site ([www.fmc.gov](http://www.fmc.gov)) or directly from the Bureau of Certification and Licensing.

The revision to section 540.7 is adopted and requires that each Certificate (Performance) expire 5 years from the date of issuance. The current rule provides that the certificate may continue in effect indefinitely. The Final Rule does not, however, require expiration of the underlying financial responsibility instruments.

This revision will assist the U.S. Customs and Border Protection to verify the validity of a certificate under 46 U.S.C. 44105, and ensure that the Commission periodically confirms PVO information previously submitted. This change harmonizes the Commission's PVO certificates with domestic and international certificates (e.g., the U.S. Coast Guard's Certificate of Inspection, those issued under The Safety of Life at Sea Convention, and the International Convention on Load Lines).<sup>13</sup> Further, the final rule also provides that the Commission, for good cause, could issue a certificate with an expiration date of less than 5 years, which creates a flexible process that permits short-term certificates to be issued to PVOs that operate from U.S. ports episodically.

NASBP supports expiration dates for each Certificate (Performance), indicating that surety bonds were not meant to be indefinite. The final rule, however, is not

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<sup>13</sup> On October 31, 1988, the International Maritime Organization (IMO) convened the International Conference on the Harmonized Systems of Survey and Certification to adopt the Protocol of 1988 relating to the International Convention for Safety of Life at Sea (SOLAS), 1974, and the Protocol of 1988 relating to the International Convention on Load Lines, 1966. By adopting these 1988 Protocols, IMO standardized the term of validity for certificates and intervals for vessel inspections required by the Conventions. These 1988 Protocols entered into force as international law on February 3, 2000. See also 65 FR 6494 (February 9, 2000).

intended to affect the underlying financial responsibility. Rather the certificate expiration provides the opportunity for the updating of each PVO's information with the Commission as well as the broader reasons indicated. However, should the PVO and its surety include an expiration date less than five years for the underlying security, the certificate could be issued with that expiration date.

The sample surety bond, guaranty, and escrow agreement are amended as contained in the NPRM and will continue to be set out in the Commission's regulations.

#### Regulatory Flexibility Act – Threshold Analysis

The Regulatory Flexibility Act of 1980, (RFA)<sup>14</sup> as modified by the Small Business Regulatory Enforcement Fairness Act (SBREFA),<sup>15</sup> requires Federal agencies to consider the impact of regulatory proposals on small entities and determine, in good faith, whether there were equally effective alternatives that would make the regulatory burden on small business more equitable.<sup>16</sup> Agencies must first conduct a threshold analysis to determine whether regulatory actions are expected to have significant economic impact on a substantial number of small entities. If the threshold analysis indicates a significant economic impact on a substantial number of small entities, an "initial regulatory flexibility analysis" must be produced and made available for public

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<sup>14</sup> Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164 (codified at 5 U.S.C. 601 et seq.).

<sup>15</sup> Small Business Regulatory Enforcement Fairness Act of 1996, Pub.L. No. 104-121, 110 Stat. 857 (codified at 5 U.S.C. §601 et seq.).

<sup>16</sup> The term "small entities" comprises small business and not-for-profit organizations that are independently owned and operated and are not dominant in their field, and governmental jurisdictions with populations of less than 50,000.

review and comment along with the proposed regulatory action. A “final regulatory flexibility analysis” that considers public comments must then be produced and made publicly available with the final regulatory action. Agencies must publish a certification of no significant impact on a substantial number of small entities if the threshold analysis does not indicate such impacts.

The threshold analysis considered the economic impact on small businesses of the rule changes in Docket 11-16: *Passenger Vessel Operator Financial Responsibility Requirements for Nonperformance of Transportation*. It outlines the proceedings; provides a brief overview of the Passenger Vessel Operator (PVO), or cruise line, industry; discusses the small PVOs affected; and evaluates the economic impact of the rule on small PVOs based on the substantial number and the significant economic impact criteria of the RFA.

Based upon the following factual basis, the threshold analysis concludes that none of the PVOs in the Commission’s program that are identified as small entities under the Small Business Act (SBA)<sup>17</sup> will be significantly economically impacted by the Final Rule. Those small PVOs are all eligible to request reductions in their current financial responsibility by substituting alternative protection based upon credit card receipts.

#### 1. Background

The Commission issued a Request for Additional Information and Comments (RFI) on February 22, 2012. Comments were submitted by four PVOs: Royal Caribbean, Carnival, American Cruise Lines, and InnerSeas Discoveries. The analysis

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<sup>17</sup> 15 U.S.C. 632. The RFA uses the definition of small business found in the Small Business Act.

compiles confidential data provided in response to the Commission's questions about their companies' operations and demonstrates the huge differences in operational scale among the respondents.

## 2. The Regulated Industry

The industry regulated under Part 540 of the Commission's regulations consists of "persons" in the U.S. who arrange, offer, advertise or provide passage on a vessel having berth or state room accommodations for 50 or more passengers and embark passengers at U.S. ports.<sup>18</sup> The industry is referred to as the U.S. cruise line industry. The North American Industry Classification System (NAICS) codes for the U.S. cruise industry include the following: 483112-Deep Sea Passenger Transportation, 483114-Coastal and Great Lakes Passenger Transportation, and 483212-Inland Water Passenger Transportation.

As of June 30, 2012, the FMC Passenger Vessel Operator program had 40 participants. The threshold analysis reviewed each of the 40 program participants along with their 2-year high UPR, amount of performance coverage, the type of instrument used, percentage of UPR protected by bonds or escrows, and the primary market segment in which they operate. The analysis determined whether a PVO meets or exceeds the SBA size standard for the NAICS codes identified.

## 3. Description of Small PVOs Affected

The SBA defines a small business as any firm that is independently owned and operated and not dominant in its field of operation. The SBA size standard for a small

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<sup>18</sup> The Commission's rules define "person" to include individuals, corporations, partnerships, associations, and other legal entities existing under or authorized by the laws of the United States or any State thereof or the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands or any territory or possession of the United States, or the laws of any foreign country. See 46 CFR 540.2 (a).

company in the U.S. cruise industry is 500 or fewer employees. For the purposes of this analysis, any operator in the PVO program that is affiliated with, or a subsidiary of, a larger entity is considered to exceed the SBA size standard. For example, a PVO that operates one vessel in the Commission's PVO program, has a 2-year high UPR of less than \$1 million, and may have fewer than 500 employees in the U.S. However, it is considered to have exceeded the SBA size standard because it is a subsidiary of a large global enterprise. Such a single vessel operator does not meet the "independently owned and operated" criteria for a small business. A total of nine operators in the PVO program are considered to have exceeded the SBA size standard by the same reasoning.

Seven PVOs were eliminated from this analysis because they have either no UPR or no financial responsibility instrument (performance) on file with the Commission. These PVOs maintain a casualty certificate and many embark passengers from U.S. ports on a very limited basis (i.e., embark very few passengers at one U.S. port on a rare occasion or perform several short-term chartered cruises once a year or every 2 or 3 years). Historically, UPR for these seven PVOs has been well under the \$15 million cap.

Staff identified nine PVOs in the program that meet the SBA size standard and are considered to be small businesses. Six of the nine small PVOs are exploration/soft adventure operators which operate U.S. flag vessels in Alaska, U.S. coastal waters, or on inland waterways. These operators would be classified in the NAICS codes of 483112-Deep Sea Passenger Transportation, 483114-Coastal and Great Lakes



Passenger Transportation, and 483212- Inland Water Passenger Transportation. Because they are U.S. flag operators, they are required to have U.S. ownership, use U.S.-built ships, and use U.S. citizens as crew members. The remaining three small PVOs are foreign flag operators operating in various U.S./foreign cruise and ferry markets using Panamanian and Bahamian flag vessels, and they are classified in NAICS code 483112-Deep Sea Passenger Transportation.

#### 4. Economic Impact of the Rule on Small PVOs

Assessing economic impact involves estimating the cost of any increased financial performance coverage. On a per-passenger basis, the cost of financial coverage can vary significantly depending on the size of the PVO. For example, the cost per passenger for a large PVO whose coverage is capped at \$15 million level can be very small. In contrast, a small PVO's coverage can be many times that of the large operator for the same time period.

##### *Increase of Financial Responsibility*

The economic impact on small PVOs depends upon the instrument used to establish financial responsibility. Five of the program's small PVOs have bonds. Based on conversations with a surety association, BCL finds that the least risky PVOs would probably pay about 0.5 percent of the instrument's face value, while the most risky would probably pay about 3 percent. These estimates were used for the baseline estimate of economic impact of the current rule. The threshold analysis shows the range of possibilities for those small PVOs using bonds. The level of coverage based on 110% UPR with the increased cap also was calculated as was the range of annual premiums.

Differences in anticipated annual premiums under the current and proposed rules were calculated. Only one operator with UPR exceeding the \$15 million cap would be expected to have increased premium costs.

One commenter provided the percentage of the bond amount that it must pay to its surety as an annual premium and advised that the surety requires it to obtain a letter of credit in an amount that is a percentage of the bond value. The PVO also provided the amount of its current letter of credit and advised that the process of obtaining the surety bond and letter of credit also incurs additional bank and legal fees.

The threshold analysis reviewed the estimated cost of increasing financial responsibility to \$30 million on the five small PVOs using bonds in comparison to their costs under the current rule using each PVO's current 2 year high UPR, its current performance coverage, the estimated cost of coverage using the .5 and 3 percentages provided by the surety association. One small PVO commented that one of the most important additional costs would be the opportunity cost of tying up additional credit availability to secure its bond.

The threshold analysis, however, indicated that the cost of coverage when the cap increases to \$30 million for one PVO may increase the average ticket price by less than one percent. The other four PVOs using bonds would experience no increase in their surety bonds as a result of the cap increase.

The threshold analysis also reviewed the remaining four small PVOs that use escrow accounts. Balances in these accounts change weekly as additional fares are deposited; cruises are completed; and the "unearned" revenue associated with the

completed cruise becomes “earned” and is withdrawn from the account. Escrow account holders are assessed administrative fees, unlike PVOs using surety bonds or guarantees that are charged premiums linked to the amount of the instrument. Administrative fees, on the other hand, are generally not based on the value of the account. Rather escrow agents or managers have fee schedules which are dependent upon the number and types of transactions or services provided. These include deposits, wire transfers, number of checks processed and issued, number of transfer payments, and documentation preparation. In addition, escrow agents may charge a monthly service fee. The new rule would not affect the basis on which administrative fees are assessed.

To determine the economic impact for these operators, the “opportunity cost”<sup>19</sup> of the capital that the operators are required to maintain in the escrow accounts (but otherwise could have used for other purposes) was calculated. For the purposes of calculating this cost, it was assumed that the small PVOs would need to obtain commercial loans to meet working capital requirements or to fund capital investments or improvements, in lieu of not being able to use the funds held in escrow. For purposes of this analysis, and because escrow account balances change frequently, the mean of the operators’ UPR reported weekly over a recent twelve month period (July 2011 through June 2012) was calculated for each operator using interest rates for short-term commercial loans.<sup>20</sup>

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<sup>19</sup> The opportunity cost of an action is the value of the foregone alternative action. Source: The MIT Dictionary of Modern Economics, 4<sup>th</sup> Edition, p. 315.

<sup>20</sup> Interest rate information for short-term loans obtained from the National Federation of Independent Business (NFIB), *NFIB Small Business Economic Trends*, July 2012, p. 14. The interest rate used assumes that the operators have good credit standing.

Because these four small PVOs have UPR levels well below the current \$15 million cap, they will not be required to obtain additional performance coverage under the regulations. As a result, these small PVOs would not be subject to any immediate additional economic impact.

#### *Additional Forms of Financial Protection*

With respect to the new provision contained in the Final Rule at 46 CFR 540(j)(ii), based on the current levels of their 2-year high UPR with respect to the required cap (both existing and proposed), it appears that all nine small PVOs may be able to demonstrate the existence of additional forms of protection. To the extent that those proposals are acceptable to the Commission, it would be expected that the elimination of coverage duplication would result in no additional economic impact for any small PVO, and may even reduce it in some cases.

#### 5. Threshold Analysis - Conclusion

Forty operators participate in the FMC's PVO program. Nine are small PVOs as defined by the SBA's small business size standards for NAICS codes of 483112-Deep Sea Passenger Transportation, 483114-Coastal and Great Lakes Passenger Transportation, and 483212- Inland Water Passenger Transportation.

With one exception, all small operators will be left unaffected economically by the rule changes, even without consideration of alternative forms of coverage. The amount of required coverage should remain the same for these operators. After the evaluation reflected in the threshold analysis, the economic impact on the one small operator does not appear likely to be significantly adverse. Should that operator not avail itself of a

reduction under the alternative form of coverage provided in the Final Rule, the compliance cost increase brought about by the rule change would increase costs per passenger by a small amount. If this cost is passed on in its entirety to the cruise passengers, it would raise that operator's average fare by less than one percent and still leave the cruise line profitable. It does not seem likely that this level of impact will drive a small PVO out of business or decrease its ability to make future capital investments or harm its competitiveness against larger firms.

However, the Final Rule would allow the Commission, on a case-by-case basis, to recognize additional protections submitted by small PVOs with UPR not exceeding 150 percent of the \$30 million cap. Most likely, the one operator that would be affected by the increased cap, should it choose to avail itself of this provision, would be required to produce less coverage and incur less cost than it does now. Consequently, the threshold analysis does not indicate that the Final Rule in this proceeding will have a significant economic impact on a substantial number of small business entities.

Even without recognition of alternative forms of coverage, the threshold analysis concludes that this rule will not have a significant economic impact on a substantial number of small entities and, therefore, the analysis recommends that the Chairman so certify pursuant to section 605(b) of the RFA.

#### The Final Rule is not a Major Rule

This rule is not a "major rule" under 5 U.S.C. 804(2).

As described in the NPRM, the collection of information requirements contained in the rule have been submitted to the Office of Management and Budget for review

under section 3504(h) of the Paperwork Reduction Act of 1980, as amended. OMB has withheld approval of the forms affected by the rule pending receipt of a summary of comments pertaining to information collection burden imposed by the rule or change made in response to comments. No comments were received relating to information collection burden of the rule.

Inasmuch as the PVOs that are subject to the Commission's passenger vessel financial responsibility regulations at 46 CFR Part 540 are already subject to requirements to submit application forms, financial responsibility instruments and periodic reports of their unearned passenger revenues, the final rule does not impose any new recordkeeping or reporting requirements on PVOs that would be "collection of information" requiring approval under the Paperwork Reduction Act, 44 U.S.C. 3501 *et seq.*

## **List of Subjects**

### 46 CFR Part 501

Administrative practice and procedure, Authority delegations, Organization and functions, Seals and insignia.

### 46 CFR Part 540

Insurance, Maritime carriers, Reporting and recordkeeping requirements, Surety bonds.

For the reasons stated in the supplementary information, the Federal Maritime Commission amends 46 CFR Parts 501 and 540 as follows.

## **PART 501—THE FEDERAL MARITIME COMMISSION—GENERAL**

1. Revise the authority citation for Part 501 to read as follows:

Authority: 5 U.S.C. 551-557, 701-706, 2903 and 6304; 31 U.S.C. 3721; 41 U.S.C. 414

and 418; 44 U.S.C. 501-520 and 3501-3520; 46 U.S.C. 301-307, 40101-41309, 42101-42109, 44101-44106; Pub. L. 89-56, 70 Stat. 195; 5 CFR Part 2638; Pub. L. 104-320, 110 Stat. 3870.

2. Revise § 501.5(g)(2) to read as follows:

**§ 501.5 Functions of the organizational components of the Federal Maritime Commission.**

\* \* \* \* \*

(g) \* \* \*

(2) Through the Office of Passenger Vessels and Information Processing, has responsibility for reviewing applications for certificates of financial responsibility with respect to passenger vessels, reviewing requests for substitution of alternative forms of financial protection, managing all activities with respect to evidence of financial responsibility for OTIs and passenger vessel owner/operators, and for developing and maintaining all Bureau database and records of OTI applicants and licensees.

\* \* \* \* \*

3. Amend § 501.26 introductory text by removing the word “redelgated” and adding the word “redelegated” in its place, and add §501.26(d) to provide as follows:

**§ 501.26 Delegation to and redelegation by Director, Bureau of Certification and Licensing.**

\* \* \* \* \*

(d) Authority to the Director, Bureau of Certification and Licensing to grant requests to substitute alternative financial responsibility pursuant to §540.9(l) of this chapter based upon existing protection available to purchases of passenger vessel transportation by

credit card by an amount up to fifty (50) percent of the passenger vessel operator's highest two-year unearned passenger revenues.

## **PART 540—PASSENGER VESSEL FINANCIAL RESPONSIBILITY**

4. The authority citation for Part 540 continues to read as follows:

Authority: 5 U.S.C. 552, 553; 31 U.S.C. 9701; 46 U.S.C. 305, 44101–44106.

5. Amend § 540.1 by revising the second sentence of paragraph (b) to read as follows:

### **§ 540.1 Scope.**

\* \* \* \* \*

(b) \* \* \* Vessels operating without the proper certificate may be denied clearance by the Department of Homeland Security and their owners may also be subject to a civil penalty of not more than \$5,000 in addition to a civil penalty of \$200 for each passage sold, such penalties to be assessed by the Federal Maritime Commission (46 U.S.C. 44101-44106, 60105).

6. Amend § 540.2 by revising paragraphs (a) and (i) to read as follows:

### **§ 540.2 Definitions.**

\* \* \* \* \*

(a) *Person* includes individuals, limited liability companies, corporations, partnerships, associations, and other legal entities existing under or authorized by the laws of the United States or any State thereof or the District of Columbia, the Commonwealth of



Puerto Rico, the Virgin Islands or any territory or possession of the United States, or the laws of any foreign country.

\* \* \* \* \*

(i) *Unearned passenger revenue* means that passenger revenue received for water transportation and all other accommodations, services, and facilities relating thereto not yet performed; this includes port fees and taxes paid, but excludes such items as airfare, hotel accommodations, and tour excursions.

\* \* \* \* \*

7. Revise § 540.4 to read as follows:

**§ 540.4 Procedure for establishing financial responsibility.**

(a) In order to comply with section 3 of Public Law 89-777 (46 U.S.C. 44101–44102, 44104–44106) enacted November 6, 1966, there must be filed with the Federal Maritime Commission an application on Form FMC-131 for a Certificate of Financial Responsibility for Indemnification of Passengers for Nonperformance of Transportation. Copies of Form FMC-131 may be obtained from the Commission's website at <http://www.fmc.gov>, or from the Bureau of Certification and Licensing, Federal Maritime Commission, Washington, DC 20573.

(b) An application for a Certificate (Performance) shall be filed with the Bureau of Certification and Licensing, Federal Maritime Commission, by the vessel owner or charterer at least 60 days in advance of the arranging, offering, advertising, or providing of any water transportation or tickets in connection therewith except that any person other than the owner or charterer who arranges, offers, advertises, or provides passage on a vessel may apply for a Certificate (Performance). Late filing of the application will

be permitted without penalty only for good cause shown.

(c) All applications and evidence required to be filed with the Commission shall be in English, and any monetary terms shall be expressed in terms of U.S. currency.

(d) The Commission shall have the privilege of verifying any statements made or any evidence submitted under the rules of this subpart.

(e) An application for a Certificate (Performance), excluding an application for the addition or substitution of a vessel to the applicant's fleet, shall be accompanied by a filing fee remittance of \$2,767. An application for a Certificate (Performance) for the addition or substitution of a vessel to the applicant's fleet shall be accompanied by a filing fee remittance of \$1,382. Administrative changes, such as the renaming of a vessel will not incur any additional fees.

(f) The application shall be signed by a duly authorized officer or representative of the applicant with a copy of evidence of his or her authority.

(g) In the event of any material change in the facts as reflected in the application, an amendment to the application shall be filed no later than fifteen (15) days following such change. For the purpose of this subpart, a material change shall be one which:

(1) Results in a decrease in the amount submitted to establish financial responsibility to a level below that required to be maintained under the rules of this subpart, or

(2) Requires that the amount to be maintained be increased above the amount submitted to establish financial responsibility.

(h) Notice of the application for issuance, denial, revocation, suspension, or modification of any such Certificate will be published on the Commission's web site at

*http://www.fmc.gov.*

8. Amend § 540.5 as follows:

- a. Revise paragraph (a)(1)(i) to read as follows; and
- b. Amend paragraph (c) by adding a sentence at the end of the paragraph to read as follows.

**§ 540.5 Insurance, guaranties, and escrow accounts.**

\* \* \* \* \*

(a) \* \* \*

(1) \* \* \* (i) Until notice in writing has been given to the assured or to the insurer and to the Bureau of Certification and Licensing at its office in Washington, DC 20573, by certified mail or courier service, \* \* \*

\* \* \* \* \*

(c) \* \* \* Copies of Form FMC-133A may be obtained from the Commission's website at *http://www.fmc.gov* or from the Bureau of Certification and Licensing.

\* \* \* \* \*

9. Amend § 540.6 by adding a sentence at the end of paragraph (a) to read as follows:

**§ 540.6 Surety bonds.**

(a) \* \* \* Copies of Form FMC-132A may be obtained from the Commission's website at

<http://www.fmc.gov> or from the Bureau of Certification and Licensing.

\* \* \* \* \*

10. Revise § 540.7 to read as follows:

**§ 540.7 Evidence of financial responsibility.**

Where satisfactory proof of financial responsibility has been established:

(a) A Certificate (Performance) covering specified vessels shall be issued evidencing the Commission's finding of adequate financial responsibility to indemnify passengers for nonperformance of water transportation.

(b) The period covered by the Certificate (Performance) shall be five (5) years, unless another termination date has been specified thereon.

11. Amend § 540.8 by revising paragraphs (a) and (b)(3) to read as follows:

**§ 540.8 Denial, revocation, suspension, or modification.**

(a) Prior to the denial, revocation, suspension, or modification of a Certificate (Performance), the Commission shall notify the applicant of its intention to deny, revoke, suspend, or modify and shall include with the notice the reason(s) for such action. If the applicant, within 20 days after the receipt of such notice, requests a hearing to show that the evidence of financial responsibility filed with the Commission does meet the rules of this subpart, such hearing shall be granted by the Commission. Regardless of a

hearing, a Certificate (Performance) shall become null and void upon cancellation or termination of the surety bond, evidence of insurance, guaranty, or escrow account.

(b) \* \* \*

(3) Failure to comply with or respond to lawful inquiries, requests for information, rules, regulations, or orders of the Commission pursuant to the rules of this subpart.

\* \* \* \* \*

12. Amend § 540.9 by revising paragraphs (c), (e), (h), (j), and (k), and adding a new paragraph (l) to read as follows:

**§ 540.9 Miscellaneous.**

\* \* \* \* \*

(c) The Commission's bond (Form FMC-132A), guaranty (Form FMC-133A), and application (Form FMC-131) forms may be obtained from the Commission's website at <http://www.fmc.gov> or from the Bureau of Certification and Licensing at its office in Washington, DC 20573.

\* \* \* \* \*

(e) Each applicant, insurer, escrow agent and guarantor shall furnish a written designation of a person in the United States as legal agent for service of process for the purposes of the rules of this subpart. Such designation must be acknowledged, in writing, by the designee and filed with the Commission. In any instance in which the designated agent cannot be served because of death, disability, or unavailability, the

Secretary, Federal Maritime Commission, will be deemed to be the agent for service of process. A party serving the Secretary in accordance with the above provision must also serve the certificant, insurer, escrow agent, or guarantor, as the case may be, by certified mail or courier service at the last known address of them on file with the Commission.

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(h) Every person who has been issued a Certificate (Performance) must submit to the Commission a semi-annual statement of any changes with respect to the information contained in the application or documents submitted in support thereof or a statement that no changes have occurred. Negative statements are required to indicate no change. These statements must cover the 6-month period of January through June and July through December, and include a statement of the highest unearned passenger vessel revenue accrued for each month in the 6-month reporting period. Such statements will be due within 30 days after the close of every such 6-month period. The reports required by this paragraph shall be submitted to the Bureau of Certification and Licensing at its office in Washington, DC 20573 by certified mail, courier service, or electronic submission.

\* \* \* \* \*

(j) The amount of: the insurance as specified in § 540.5(a), the escrow account as specified in § 540.5(b), the guaranty as specified in § 540.5(c), or the surety bond as specified in § 540.6 shall not be required to exceed \$15 million for one year after April 2, 2013. Twelve (12) months after April 2, 2013, the amount shall not exceed \$22 million,

and twenty four (24) months after April 2, 2013, the amount shall not exceed \$30 million. Every two years, on the anniversary after the cap on required financial responsibility reaches \$30 million, the cap shall automatically adjust to the nearest \$1 million based on changes as reflected in the U.S. Bureau of Labor Statistics' Consumer Price Index. The Bureau of Certification and Licensing will determine the amount of each adjustment and transmit that information to the Secretary of the Federal Maritime Commission for publication on the Commission's website ([www.fmc.gov](http://www.fmc.gov)) and in the *Federal Register* with an effective date that is no less than sixty (60) days after *Federal Register* publication.

(k) Every person in whose name a Certificate (Performance) has been issued shall be deemed to be responsible for any unearned passage money or deposits held by its agents or any other person authorized by the certificant to sell the certificant's tickets. Certificants shall promptly notify the Commission of any arrangements, including charters and subcharters, made by it or its agent with any person pursuant to which the certificant does not assume responsibility for all passenger fares and deposits collected by such person or organization and held by such person or organization as deposits or payment for services to be performed by the certificant. If responsibility is not assumed by the certificant, the certificant also must inform such person or organization of the certification requirements of Public Law 89-777 and not permit use of its vessel, name or tickets in any manner unless and until such person or organization has obtained the requisite Certificate (Performance) from the Commission. Failure to follow the procedures in this paragraph means the certificant shall retain full financial responsibility

for indemnification of passengers for nonperformance of the transportation.

(l) *Requests to substitute alternative financial responsibility.* (1) A certificant whose unearned passenger revenue at no time for the two immediately prior fiscal years has exceeded 150% of the required cap may submit a request to the Director, Bureau of Certification and Licensing, to substitute alternative forms of financial protection to evidence the financial responsibility as otherwise provided in this part.

(2) The Commission will consider such requests on a case-by-case basis.

(3) The request must include copies of the requesting PVO's most recently available annual and quarterly financial and income statements. Other documents and information in support of its request may also be submitted.

(4) For requests based upon the already existing protections available to credit card purchases of passenger vessel transportation, the requesting PVO must supply the following information for the most recent twelve months preceding the request: Total deposits and payments received for passenger vessel transportation; Credit card receipt totals; Copy of the PVO's policy(ies) governing payments by passengers (i.e., deposits and the number of days prior to sailing the passenger must make final payment).

(5) In determining whether and to what level to reduce the required amount, the Commission may consider the extent to which other statutory requirements provide relevant protections, the certificant's financial data, and other specific facts and circumstances.

(6) For PVOs with payment policies that provide for final payment for the passenger vessel transportation no later than 60 days before the vessel's sailing date, requests



based upon credit card receipts may be granted by the Commission permitting a reduction in the financial responsibility otherwise required under this Part. The amount of such a reduction will be established by determining the proportion that the PVO's total credit card receipts bears to its total receipts and applying one half of that percentage to the PVO's highest two-year UPR.

(7) The Bureau of Certification and Licensing may request additional information as may assist it in considering the request.

(8) Where a request is granted, the alternative financial responsibility shall remain in effect until the PVO's Certificate (Performance) expires under § 540.7(b) or until the Director, Bureau of Certification and Licensing determines otherwise based upon changing information pursuant to this paragraph or paragraph (l)(5) of this section. Additional information may be requested at any time by the Commission or BCL from a PVO whose request under this section has been granted.

13. Remove Form FMC-131 to Subpart A of Part 540.

14. Revise Form FMC-132A to Subpart A of Part 540 to read follows:

FORM FMC-132A TO SUBPART A OF PART 540

FORM FMC-132A  
FEDERAL MARITIME COMMISSION  
Passenger Vessel Surety Bond (Performance)

Surety Co. Bond No. \_\_\_\_\_  
FMC Certificate No. \_\_\_\_\_

Know all men by these presents, that we \_\_\_\_\_ (Name of applicant),  
of \_\_\_\_\_ (City), \_\_\_\_\_ (State and country), as Principal  
(hereinafter called Principal), and \_\_\_\_\_ (Name of surety), a company created

and existing under the laws of \_\_\_\_\_ (State and country) and authorized to do business in the United States as Surety (hereinafter called Surety) are held and firmly bound unto the United States of America in the penal sum of \_\_\_\_\_, for which payment, well and truly to be made, we bind ourselves and our heirs, executors, administrators, successors, and assigns, jointly and severally, firmly by these presents. Whereas the Principal intends to become a holder of a Certificate (Performance) pursuant to the provisions of subpart A of part 540 of title 46, Code of Federal Regulations and has elected to file with the Federal Maritime Commission such a bond to insure financial responsibility and the supplying transportation and other services subject to subpart A of part 540 of title 46, Code of Federal Regulations, in accordance with the ticket contract between the Principal and the passenger, and

Whereas this bond is written to assure compliance by the Principal as an authorized holder of a Certificate (Performance) pursuant to subpart A of part 540 of title 46, Code of Federal Regulations, and shall inure to the benefit of any and all passengers to whom the Principal may be held legally liable for any of the damages herein described. Now, therefore, the condition of this obligation is such that if the Principal shall pay or cause to be paid to passengers any sum or sums for which the Principal may be held legally liable by reason of the Principal's failure faithfully to provide such transportation and other accommodations and services in accordance with the ticket contract made by the Principal and the passenger while this bond is in effect for the supplying of transportation and other services pursuant to and in accordance with the provisions of subpart A of part 540 of title 46, Code of Federal Regulations, then this obligation shall be void, otherwise, to remain in full force and effect.

The liability of the Surety with respect to any passenger shall not exceed the passage price paid by or on behalf of such passenger. The liability of the Surety shall not be discharged by any payment or succession of payments hereunder, unless and until such payment or payments shall amount in the aggregate to the penalty of the bond, but in no event shall the Surety's obligation hereunder exceed the amount of said penalty. The Surety agrees to furnish written notice to the Federal Maritime Commission forthwith of all suits filed, judgments rendered, and payments made by said Surety under this bond.

This bond is effective the \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_, 12:01 a.m., standard time at the address of the Principal as stated herein and shall continue in force until terminated as hereinafter provided. The Principal or the Surety may at any time terminate this bond by written notice sent by certified mail, courier service, or other electronic means such as email and fax to the other and to the Federal Maritime Commission at its office in Washington, D.C., such termination to become effective thirty (30) days after actual receipt of said notice by the Commission, except that no such termination shall become effective while a voyage is in progress. The Surety shall not be liable hereunder for any refunds due under ticket contracts made by the Principal for the supplying of transportation and other services after the termination of this bond as herein provided, but such termination shall not affect the liability of the Surety

hereunder for refunds arising from ticket contracts made by the Principal for the supplying of transportation and other services prior to the date such termination becomes effective.

The underwriting Surety will promptly notify the Director, Bureau of Certification and Licensing, Federal Maritime Commission, Washington, DC 20573, of any claim(s) or disbursements against this bond.

In witness whereof, the said Principal and Surety have executed this instrument on \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_.

**PRINCIPAL**

Name \_\_\_\_\_

By \_\_\_\_\_  
(Signature and title)

Witness \_\_\_\_\_

**SURETY**

[SEAL]  
Name \_\_\_\_\_

By \_\_\_\_\_  
(Signature and title)

Witness \_\_\_\_\_

Only corporations or associations of individual insurers may qualify to act as surety, and they must establish to the satisfaction of the Federal Maritime Commission legal authority to assume the obligations of surety and financial ability to discharge them.

15. Revise Form FMC-133A to Subpart A of Part 540 to read as follows:

FORM FMC-133A TO SUBPART A OF PART 540

FORM FMC-133A  
FEDERAL MARITIME COMMISSION  
Guaranty in Respect of Liability for Nonperformance, Section 3 of the Act

Guaranty No. \_\_\_\_\_  
FMC Certificate No. \_\_\_\_\_

1. Whereas \_\_\_\_\_ (Name of applicant) (Hereinafter referred to as the "Applicant") is the Owner or Charterer of the passenger Vessel(s) specified in the annexed Schedule ("the Vessels"), which are or may become engaged in voyages to or from United States ports, and the Applicant desires to establish its financial responsibility in accordance with section 3 of Pub. L. 89-777, 89th Congress, approved November 6, 1966 ("the Act") then, provided that the Federal Maritime Commission ("FMC") shall have accepted, as sufficient for that purpose, the Applicant's application, supported by this Guaranty, and provided that FMC shall issue to the Applicant a Certificate (Performance) ("Certificate"), the undersigned Guarantor hereby guarantees to discharge the Applicant's legal liability to indemnify the passengers of the Vessels for nonperformance of transportation within the meaning of section 3 of the Act, in the event that such legal liability has not been discharged by the Applicant within 21 days after any such passenger has obtained a final judgment (after appeal, if any) against the Applicant from a United States Federal or State Court of competent jurisdiction, or has become entitled to payment of a specified sum by virtue of a compromise settlement agreement made with the Applicant, with the approval of the Guarantor, whereby, upon payment of the agreed sum, the Applicant is to be fully, irrevocably and unconditionally discharged from all further liability to such passenger for such nonperformance.

2. The Guarantor's liability under this Guaranty in respect to any passenger shall not exceed the amount paid by such passenger; and the aggregate amount of the Guarantor's liability under this Guaranty shall not exceed \$\_\_\_\_\_.

3. The Guarantor's liability under this Guaranty shall attach only in respect of events giving rise to a cause of action against the Applicant, in respect of any of the Vessels, for nonperformance of transportation within the meaning of Section 3 of the Act, occurring after the Certificate has been granted to the Applicant, and before the expiration date of this Guaranty, which shall be the earlier of the following dates:

(a) The date whereon the Certificate is withdrawn, or for any reason becomes invalid or ineffective; or

(b) The date 30 days after the date of receipt by FMC of notice in writing delivered by certified mail, courier service or other electronic means such as email and fax, that the Guarantor has elected to terminate this Guaranty except that:

(i) If, on the date which would otherwise have been the expiration date under the foregoing provisions (a) or (b) of this Clause 3, any of the Vessels is on a voyage whereon passengers have been embarked at a United States port, then the expiration date of this Guaranty shall, in respect of such Vessel, be postponed to the date on which the last passenger on such voyage shall have finally disembarked; and

(ii) Such termination shall not affect the liability of the Guarantor for refunds arising from ticket contracts made by the Applicant for the supplying of transportation and other services prior to the date such termination becomes effective.

4. If, during the currency of this Guaranty, the Applicant requests that a vessel owned or operated by the Applicant, and not specified in the annexed Schedule, should become subject to this Guaranty, and if the Guarantor accedes to such request and so notifies FMC in writing or other electronic means such as email and fax, then, provided that within 30 days of receipt of such notice, FMC shall have granted a Certificate, such Vessel shall thereupon be deemed to be one of the Vessels included in the said Schedule and subject to this Guaranty.

5. The Guarantor hereby designates \_\_\_\_\_, with offices at \_\_\_\_\_, as the Guarantor's legal agent for service of process for the purposes of the Rules of the Federal Maritime Commission, subpart A of part 540 of title 46, Code of Federal Regulations, issued under Section 3 of Pub. L. 89-777 (80 Stat. 1357, 1358), entitled "Security for the Protection of the Public."

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(Place and Date of Execution)

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(Type Name of Guarantor)

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(Type Address of Guarantor)

By \_\_\_\_\_  
(Signature and Title)

Schedule of Vessels Referred to in Clause 1

Vessels Added to This Schedule in Accordance With Clause 4

16. Revise Appendix A to Subpart A of Part 540 to read as follows:

APPENDIX A TO SUBPART A OF PART 540—EXAMPLE OF ESCROW AGREEMENT FOR USE UNDER 46  
CFR 540.5( b )

#### ESCROW AGREEMENT

THIS ESCROW AGREEMENT, made as of this \_\_\_ day of (month & year), by and between (Customer), a corporation/company having a place of business at ("Customer") \_\_\_\_\_ and (Banking Institution name & address) a banking corporation, having a place of business at ("Escrow Agent").

Witnesseth:

WHEREAS, Customer wishes to establish an escrow account in order to provide for the indemnification of passengers in the event of non-performance of water transportation to which such passengers would be entitled, and to establish Customer's financial responsibility therefore; and

WHEREAS, Escrow Agent wishes to act as Escrow Agent of the escrow account established hereunder;

NOW, THEREFORE, in consideration of the premises and covenants contained herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto agree as follows:

1. Customer has established on (month, & year) (the "Commencement Date") an escrow account with the Escrow Agent which escrow account shall hereafter be governed by the terms of this Agreement (the "Escrow Account"). Escrow Agent shall maintain the Escrow Account in its name, in its capacity as Escrow Agent.

2. Customer will determine, as of the date prior to the Commencement Date, the amount of unearned passenger revenue, including any funds to be transferred from any predecessor Escrow Agent. Escrow Agent shall have no duty to calculate the amount of unearned passenger revenue. Unearned Passenger Revenues are defined as that passenger revenue received for water transportation and all other accommodations, services and facilities relating thereto not yet performed. 46 C.F.R. 540.2 (i).

3. Customer will deposit on the Commencement Date into the Escrow Account cash in an amount equal to the amount of Unearned Passenger Revenue determined under Paragraph 2 above plus a cash amount ("the Fixed Amount") equal to (10 percent of the Customer's highest Unearned Passenger Revenue for the prior two fiscal years. For periods on or after (year of agreement (2009)), the Fixed Amount shall be determined by the Commission on an annual basis, in accordance with 46 CFR Part 540.

4. Customer acknowledges and agrees that until such time as a cruise has been completed and Customer has taken the actions described herein, Customer shall not be entitled, nor shall it have any interest in any funds deposited with Escrow Agent to the extent such funds represent Unearned Passenger Revenue.

5. Customer may, at any time, deposit additional funds consisting exclusively of Unearned Passenger Revenue and the Fixed Amount, into the Escrow Account and Escrow Agent shall accept all such funds for deposit and shall manage all such funds pursuant to the terms of this Agreement.

6. After the establishment of the Escrow Account, as provided in Paragraph 1, Customer shall on a weekly basis on each (identify day of week), or if Customer or Escrow Agent is not open for business on (identify day of week) then on the next

business day that Customer and Escrow Agent are open for business recompute the amount of Unearned Passenger Revenue as of the close of business on the preceding business day (hereinafter referred to as the "Determination Date") and deliver a Recomputation Certificate to Escrow Agent on such date. In each such weekly recomputation Customer shall calculate the amount by which Unearned Passenger Revenue has decreased due to (i) the cancellation of reservations and the corresponding refund of monies from Customer to the persons or entities canceling such reservations; (ii) the amount which Customer has earned as revenue as a result of any cancellation fee charged upon the cancellation of any reservations; (iii) the amount which Customer has earned due to the completion of cruises; and (iv) the amount by which Unearned Passenger Revenue has increased due to receipts from passengers for future water transportation and all other accommodations, services and facilities relating thereto and not yet performed.

The amount of Unearned Passenger Revenue as recomputed shall be compared with the amount of Unearned Passenger Revenue for the immediately preceding period to determine whether there has been a net increase or decrease in Unearned Passenger Revenue. If the balance of the Escrow Account as of the Determination Date exceeds the sum of the amount of Unearned Passenger Revenue, as recomputed, plus the Fixed Amount then applicable, then Escrow Agent shall make any excess funds in the Escrow Account available to Customer. If the balance in the Escrow Account as of the Determination Date is less than the sum of the amount of Unearned Passenger Revenue, as recomputed, plus an amount equal to the Fixed Amount, Customer shall deposit an amount equal to such deficiency with the Escrow Agent. Such deposit shall be made in immediately available funds via wire transfer or by direct transfer from the Customer's U.S. Bank checking account before the close of business on the next business day following the day on which the Recomputation Certificate is received by Escrow Agent. The Escrow Agent shall promptly notify the Commission within two business days any time a deposit required by a Recomputation Certificate delivered to the Escrow Agent is not timely made.

7. Customer shall furnish a Recomputation Certificate, in substantially the form attached hereto as Annex 1, to the Federal Maritime Commission (the "Commission") and to the Escrow Agent setting forth the weekly recomputation of Unearned Passenger Revenue required by the terms of Paragraph 6 above. Customer shall mail or fax to the Commission and deliver to the Escrow Agent the required Recomputation Certificate before the close of business on the business day on which Customer recomputes the amount of Unearned Passenger Revenue. Notwithstanding any other provision herein to the contrary, Escrow Agent shall not make any funds available to Customer out of the Escrow Account because of a decrease in the amount of Unearned Passenger Revenue or otherwise, until such time as Escrow Agent receives the above described Recomputation Certificate from Customer, which Recomputation Certificate shall include the Customer's verification certification in the form attached hereto as Annex 1. The copies of each Recomputation Certificate to be furnished to the Commission shall be mailed to the Commission at the address provided in Paragraph 25 herein. If copies

are not mailed to the Commission, faxed or e-mailed copies shall be treated with the same legal effect as if an original signature was furnished. No repayment of the Fixed Amount may be made except upon approval of the Commission.

Within fifteen (15) days after the end of each calendar month, Escrow Agent shall provide to Customer and to the Commission at the addresses provided in Paragraph 25 below, a comprehensive statement of the Escrow Account. Such statement shall provide a list of assets in the Escrow Account, the balance thereof as of the beginning and end of the month together with the original cost and current market value thereof, and shall detail all transactions that took place with respect to the assets and investments in the Escrow Account during the preceding month.

8. At the end of each quarter of Customer's fiscal year, Customer shall cause the independent auditors then acting for it to conduct an examination in accordance with generally accepted auditing standards with respect to the weekly Recomputation Certificates furnished by Customer of the Unearned Passenger Revenues and the amounts to be deposited in the Escrow Account and to express their opinion within forty-five (45) days after the end of such quarter as to whether the calculations at the end of each fiscal quarter are in accordance with the provisions of Paragraph 6 of this Agreement. The determination of Unearned Passenger Revenue of such independent auditors shall have control over any computation of Unearned Passenger Revenue by Customer in the event of any difference between such determinations. To the extent that the actual amount of the Escrow Account is less than the amount determined by such independent auditors to be required to be on deposit in the Escrow Account, Customer shall immediately deposit an amount of cash into the Escrow Account sufficient to cause the balance of the Escrow Account to equal the amount determined to be so required. Such deposit shall be completed no later than the business day after receipt by the Escrow Agent of the auditor's opinion containing the amount of such deficiency.

The opinion of such independent auditors shall be furnished by such auditors directly to Customer, to the Commission and to the Escrow Agent at their addresses contained in this Agreement. In the event that a required deposit to the Escrow Agent is not made within one Business Day after receipt of an auditor's report or a Recomputation Certificate, Escrow Agent shall send notification to the Commission within the next two Business Days.

9. Escrow Agent shall invest the funds in the Escrow Account in Qualified Investments as directed by Customer in its sole and absolute discretion. "Qualified Investments" means, to the extent permitted by applicable law:

(a) Government obligations or obligations of any agency or instrumentality of the United States of America;

(b) Commercial paper issued by a United States company rated in the two highest



numerical "A" categories (without regard to further gradation or refinement of such rating category) by Standard & Poor's Corporation, or in the two highest numerical "Prime" categories (without regard to further gradation or refinement of such rating) by Moody's Investor Services, Inc.;

(c) Certificates of deposit and money market accounts issued by any United States bank, savings institution or trust company, including the Escrow Agent, and time deposits of any bank, savings institution or trust company, including the Escrow Agent, which are fully insured by the Federal Deposit Insurance Corporation;

(d) Corporate bonds or obligations which are rated by Standard & Poor's Corporation or Moody's Investors Service, Inc. in one of their three highest rating categories (without regard to any gradation or refinement of such rating category by a numerical or other modifier); and

(e) Money market funds registered under the Federal Investment Company Act of 1940, as amended, and whose shares are registered under the Securities Act of 1933, as amended, and whose shares are rated "AAA", "AA+" or "AA" by Standard & Poor's Corporation.

10. All interest and other profits earned on the amounts placed in the Escrow Account shall be credited to Escrow Account.

11. This Agreement has been entered into by the parties hereto, and the Escrow Account has been established hereunder by Customer, to establish the financial responsibility of Customer as the owner, operator or charterer of the passenger vessel(s) (see Exhibit A), in accordance with Section 3 of Public Law 89-777, 89<sup>th</sup> Congress, approved November 6, 1966 (the "Act"). The Escrow Account shall be held by Escrow Agent in accordance with the terms hereof, to be utilized to discharge Customer's legal liability to indemnify the passengers of the named vessel(s) for non-performance of transportation within the meaning of Paragraph 3 of the Act. The Escrow Agent shall make indemnification payments pursuant to written instructions from Customer, on which the Escrow Agent may rely, or in the event that such legal liability has not been discharged by Customer within twenty-one (21) days after any such passenger has obtained a final judgment (after appeal, if any) against Customer from a United States Federal or State Court of competent jurisdiction the Escrow Agent is authorized to pay funds out of the Escrow Account, after such twenty-one day period, in accordance with and pursuant to the terms of an appropriate order of a court of competent jurisdiction on receipt of a certified copy of such order.

As further security for Customer's obligation to provide water transportation to passengers holding tickets for transportation on the passenger vessel(s) (see Exhibit A) Customer will pledge to each passenger who has made full or partial payment for future passage on the named vessel(s) an interest in the Escrow Account equal to such payment. Escrow Agent is hereby notified of and acknowledges such pledges.

Customers' instructions to Escrow Agent to release funds from the Escrow Account as described in this Agreement shall constitute a certification by Customer of the release of pledge with respect to such funds due to completed, canceled or terminated cruises. Furthermore, Escrow Agent agrees to hold funds in the Escrow Account until directed by Customer or a court order to release such funds as described in this Agreement. Escrow Agent shall accept instructions only from Customer, acting on its own behalf or as agent for its passengers, and shall not have any obligations at any time to act pursuant to instructions of Customer's passengers or any other third parties except as expressly described herein. Escrow Agent hereby waives any right of offset to which it is or may become entitled with regard to the funds on deposit in the Escrow Account which constitute Unearned Passenger Revenue.

12. Customer agrees to provide to the Escrow Agent all information necessary to facilitate the administration of this Agreement and the Escrow Agent may rely upon any information so provided.

13. Customer hereby warrants and represents that it is a corporation in good standing in its State of organization and that is qualified to do business in the State of . Customer further warrants and represents that (i) it possesses full power and authority to enter into this Agreement and fulfill its obligations hereunder and (ii) that the execution, delivery and performance of this Agreement have been authorized and approved by all required corporate actions.

14. Escrow Agent hereby warrants and represents that it is a national banking association in good standing. Escrow Agent further warrants and represents that (i) it has full power and authority to enter into this Agreement and fulfill its obligations hereunder and (ii) that the execution, delivery and performance of this Agreement have been authorized and approved by all required corporate actions.

15. This Agreement shall have a term of one (1) year and shall be automatically renewed for successive one (1) year terms unless notice of intent not to renew is delivered to the other party to this Agreement and to the Commission at least 90 days prior to the expiration of the current term of this Agreement. Notice shall be given by certified mail to the parties at the addresses provided in Paragraph 25 below. Notice shall be given by certified mail to the Commission at the address specified in this Agreement.

16. (a) Customer hereby agrees to indemnify and hold harmless Escrow Agent against any and all claims, losses, damages, liabilities, cost and expenses, including litigation, arising hereunder, which might be imposed or incurred on Escrow Agent for any acts or omissions of the Escrow Agent or Customer, not caused by the negligence or willful misconduct of the Escrow Agent. The indemnification set forth herein shall survive the resignation or removal of the Escrow Agent and the termination of this agreement.

(b) In the event of any disagreement between parties which result in adverse claims with respect to funds on deposit with Escrow Agent or the threat thereof, Escrow Agent may refuse to comply with any demands on it with respect thereto as long as such disagreement shall continue and in so refusing, Escrow Agent need not make any payment and Escrow Agent shall not be or become liable in any way to Customer or any third party (whether for direct, incidental, consequential damages or otherwise) for its failure or refusal to comply with such demands and it shall be entitled to continue so to refrain from acting and so refuse to act until such conflicting or adverse demands shall finally terminate by mutual written agreement acceptable to Escrow Agent or by a final, non-appealable order of a court of competent jurisdiction.

17. Escrow Agent shall be entitled to such compensation for its services hereunder as may be agreed upon from time to time by Escrow Agent and Customer and which shall initially be set forth in a separate letter agreement between Escrow Agent and Customer. This Agreement shall not become effective until such letter agreement has been executed by both parties hereto and confirmed in writing to the Commission.

18. Customer may terminate this Agreement and engage a successor escrow agent, after giving at least 90 days written termination notice to Escrow Agent prior to terminating Escrow Agent if such successor agent is a commercial bank whose passbook accounts are insured by the Federal Deposit Insurance Corporation and such successor agrees to the terms of this agreement, or if there is a new agreement then such termination shall not be effective until the new agreement is approved in writing by the Commission. Upon giving the written notice to Customer and the Commission, Escrow Agent may terminate any and all duties and obligations imposed on Escrow Agent by this Agreement effective as of the date specified in such notice, which date shall be at least 90 days after the date such notice is given. All escrowed funds as of the termination date specified in the notice shall be turned over to the successor escrow agent, or if no successor escrow agent has been named within 90 days after the giving of such notice, then all such escrowed funds for sailing scheduled to commence after the specified termination date shall be returned to the person who paid such passage fares upon written approval of the Commission. In the event of any such termination where the Escrow Agent shall be returning payments to the passengers, then Escrow Agent shall request from Customer a list of passenger names, addresses, deposit/fare amounts and other information needed to make refunds. On receipt of such list, Escrow Agent shall return all passage fares held in the Escrow Account as of the date of termination specified in the notice to the passengers, excepting only amounts Customer is entitled to receive pursuant to the terms of this Agreement for cruises completed through the termination date specified in the notice, and all interest which shall be paid to Customer.

In the event of termination of this Agreement and if alternative evidence of financial responsibility has been accepted by the Commission and written evidence satisfactory to Escrow Agent of the Commission's acceptance is presented to Escrow Agent, then Escrow Agent shall release to Customer all passage fares held in the Escrow Account

as of the date of termination specified in the notice. In the event of any such termination where written evidence satisfactory to Escrow Agent of the Commission's acceptance has not been presented to Escrow Agent, then Escrow Agent shall request from Customer a list of passenger names, addresses, deposit/fare amounts and other information needed to make refunds. On receipt of such list, Escrow Agent shall return all passage fares held in the Escrow Account as of the date of termination specified in the notice to the passengers, excepting only amounts Customer is entitled to receive pursuant to the terms of this Agreement for cruises completed through the termination date specified in the notice, and all interest which shall be paid to Customer. Upon termination, Customer shall pay all costs and fees previously earned or incurred by Escrow Agent through the termination date.

19. Neither Customer nor Escrow Agent shall have the right to sell, pledge, hypothecate, assign, transfer or encumber funds or assets in the Escrow Account except in accordance with the terms of this Agreement.

20. This Agreement is for the benefit of the parties hereto and, accordingly, each and every provision hereof shall be enforceable by any or each or both of them. Additionally, this Agreement shall be enforceable by the Commission. However, this Agreement shall not be enforceable by any other party, person or entity whatsoever.

21. (a) No amendments, modifications or other change in the terms of this Agreement shall be effective for any purpose whatsoever unless agreed upon in writing by Escrow Agent and Customer and approved in writing by the Commission.

(b) No party hereto may assign its rights or obligations hereunder without the prior written consent of the other, and unless approved in writing by the Commission. The merger of Customer with another entity or the transfer of a controlling interest in the stock of Customer shall constitute an assignment hereunder for which prior written approval of the Commission is required, which approval shall not be unreasonably withheld.

22. The foregoing provisions shall be binding upon undersigned, their assigns, successors and personal representative.

23. The Commission shall have the right to inspect the books and records of the Escrow Agent and those of Customer as related to the Escrow Account. In addition, the Commission shall have the right to seek copies of annual audited financial statements and other financial related information.

24. All investments, securities and assets maintained under the Escrow Agreement will be physically located in the United States.

25. Notices relating to this Agreement shall be sent to Customer at (address) and to Escrow Agent at (address) or to such other address as any party hereto may hereafter

designate in writing. Any communication sent to the Commission or its successor organization shall be sent to the following address: Bureau of Certification and Licensing, Federal Maritime Commission, 800 North Capitol N.W., Washington, D.C. 20573-0001.

26. This agreement may be executed in any number of counterparts, each of which shall be deemed to be an original and all of which when taken together shall constitute one and the same instrument.

27. This Agreement is made and delivered in, and shall be construed in accordance with the laws of the State of \_\_\_\_\_ without regard to the choice of law rules.

IN WITNESS WHEREOF, the undersigned have each caused this Agreement to be executed on their behalf as of the date first above written.

By: \_\_\_\_\_  
Title: \_\_\_\_\_

By: \_\_\_\_\_  
Title: \_\_\_\_\_

#### EXHIBIT A

ESCROW AGREEMENT, dated \_\_\_\_\_ by and between (Customer) and (Escrow Agent).

Passenger Vessels Owned or Chartered

#### ANNEX 1

#### RECOMPUTATION CERTIFICATE

To: Federal Maritime Commission

And To:  ("Bank")

The undersigned, the Controller of \_\_\_\_\_ hereby furnishes this Recomputation Certificate pursuant to the terms of the Escrow Agreement dated \_\_\_\_\_, between the Customer and  ("Bank"). Terms herein shall have the same definitions as those in such Escrow Agreement and Federal Maritime Commission regulations.

I. Unearned Passenger Revenue as of  ("Date") was:  
\$ \_\_\_\_\_

a. Additions to unearned Passenger Revenue since such date were:

1. Passenger Receipts: \$ \_\_\_\_\_
2. Other  (Specify) : \$ \_\_\_\_\_
3. Total Additions: \$ \_\_\_\_\_

b. Reductions in Unearned Passenger Revenue since such date were:

1. Completed Cruises: \$ \_\_\_\_\_
2. Refunds and Cancellations: \$ \_\_\_\_\_
3. Other  (Specify) : \$ \_\_\_\_\_
4. Total Reductions: \$ \_\_\_\_\_

II. Unearned Passenger Revenue as of the date  
Of this Recomputation Certificate is: \$ \_\_\_\_\_  
a. Excess Escrow Amount \$ \_\_\_\_\_

III. Plus the Required Fixed Amount: \$ \_\_\_\_\_

IV. Total Required in Escrow: \$ \_\_\_\_\_

V. Current Balance in Escrow Account: \$ \_\_\_\_\_

VI. Amount to be Deposited in Escrow Account: \$ \_\_\_\_\_

VII. Amount of Escrow Account available to Operator: \$ \_\_\_\_\_

VIII. I declare under penalty of perjury that the above information is true and correct.

Dated: \_\_\_\_\_

\_\_\_\_\_  
(Signature)  
Name: Title:

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(Signature)

Name:

Title:

By the Commission.

Karen V. Gregory  
Secretary

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